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January 29, 2003

EX PARTE – Via Electronic Filing

Ms. Marlene Dortch
Secretary
Federal Communications Commission
The Portals
445 12th Street, S.W.
Washington, DC 20554

Re: CC Docket Nos. 01-338, 96-98, and 98-147

Dear Ms. Dortch:

Attached for inclusion in the record of this proceeding is a letter to Chairman Powell and the commissioners responding to Verizon's submission of January 21 on the role of the state commissions in determining the price for network elements unbundled pursuant to section 271.

In accordance with FCC rule 1.49(f), this *ex parte* letter and attachment are being filed electronically pursuant to FCC Rule 1.1206(b)(1).

Sincerely,

/s/

Christopher J. Wright
Counsel Z-Tel Communications, Inc.

cc:

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January 29, 2003

Ex Parte

Honorable Michael K. Powell
Chairman
Honorable Kathleen Q. Abernathy
Honorable Michael J. Copps
Honorable Kevin J. Martin
Honorable Jonathan S. Adelstein
Commissioners
Federal Communications Commission
445 12th Street, S.W., Room 8-B201
Washington, DC 20554

Re: Verizon's submission of January 21 on the role of the state commissions in determining the price for network elements unbundled pursuant to section 271, CC Docket Nos. 01-338, 96-98, and 98-147

Dear Chairman Powell and Commissioners:

Verizon contended in a recent letter that "when the Commission removes a network element from the list of those that must be unbundled for purposes of § 251 ... [a] state commission has absolutely no jurisdiction to require an incumbent to provide access to such a network element at a forward-looking price."[1] That contention is wrong. While the 1996 Telecommunications Act is unclear on many matters, it plainly requires Bell Operating Companies that have authorization to provide long-distance service to provide unbundled access to the network elements comprising the platform at cost-based rates. It also is clear that the BOCs must do so pursuant to interconnection agreements, the terms of which are determined by state commissions when the parties cannot agree.

1. *The BOCs are required to lease the platform of network elements at cost-based rates.* The statutory basis for the conclusion that state commissions have authority to order the BOCs to provide loops, transport, switching, and signaling at cost-based rates is

[1] Letter of January 21, 2003, from Michael E. Glover, Verizon, to Marlene H. Dortch at 7 ("*Verizon letter*").

straightforward. First, the section 271 checklist requires BOCs that provide long-distance service to unbundle each of those four network elements. Second, section 252(a)(1) provides that interconnection agreements "shall include a detailed schedule of itemized charges for ... network elements included in the agreement." And third, section 252(c)(2) directs state commissions arbitrating interconnection agreements to "establish any rates for ... network elements according to subsection (d)." Subsection (d), of course, provides that rates for network elements must be cost-based; it was construed by the Commission to call for TELRIC pricing and that determination was upheld by the Supreme Court over the BOCs' jurisdictional and substantive objections.[2]

If that were not clear enough, the legislative history and the Supreme Court's decisions leave no room for doubt. The Senate Report accompanying the bill that set forth the checklist expressly tied the requirements of section 271 to the section 251/252 process: "The Committee does not intend the competitive checklist to be a limitation on the interconnection requirements contained in section 251. Rather, the Committee intends the competitive checklist to set forth what must, at a minimum, be provided by a Bell operating company in any interconnection agreement approved under section 251."[3] In upholding TELRIC on the merits, the Supreme Court stated that Congress enacted an innovative rate-setting approach governing network elements "to give aspiring competitors every possible incentive to enter local retail telephone markets, short of confiscating the incumbents' property."[4] The Court relied on legislative history relating to section 271 to support its holding that network elements are appropriately leased at TELRIC rates. In particular, it emphasized Senator Breaux's statement to the BOCs – made in describing the checklist requirements – that, in order to "jump-start" competition: "this legislation says you will not control much of anything. You will have to allow for nondiscriminatory access on an unbundled basis to the network functions and services of the Bell operating companies network that is at least equal in type, quality, and price to the access [a] Bell operating company affords to itself."[5]

Accordingly, the statutory text, its legislative history, and the discussion of congressional purpose emphasized by the Supreme Court compel the conclusion that BOCs offering long-distance service must provide unbundled access to the network elements listed on the checklist at cost-based rates and that any disagreement about the availability of network elements and rates is to be arbitrated by the state commissions.

Moreover, the statute expressly and doubly protects state authority to establish additional unbundling requirements. Section 251(d)(3) ("preservation of state access regulations") provides that the FCC "shall not preclude the enforcement of any

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[2] *AT&T Corp. v. FCC*, 525 U.S. 366 (1999) (rejecting the BOCs' jurisdictional arguments); *Verizon Communications Inc. v. FCC*, 122 S. Ct. 1646 (2002) (rejecting the BOCs' substantive arguments).

[3] S. Rep. 104-23, 104th Cong., 1st Sess. 43 (1995).

[4] *Verizon*, *supra*, 122 S. Ct. at 1661.

[5] 141 Cong. Rec. 15572, *quoted in Verizon*, *supra*, 122 S. Ct. at 1661.

regulation, order, or policy of a State commission that ... establishes access and interconnection obligations of local exchange carriers" and section 252(e)(3) ("preservation of authority") provides that "nothing in this section shall prohibit a State commission from establishing or enforcing other requirements of State law in its review of an [interconnection] agreement." The Eighth Circuit held, in a decision that binds the Commission, that "the FCC's belief that merely an inconsistency between a state rule and a Commission regulation under section 251 is sufficient for the FCC to preempt the state rule, is an unreasonable interpretation of the statute in light of subsection 251(d)(3) and the structure of the Act."[6]

In addition, any attempt to preempt the states on the ground that requiring the BOCs to unbundle the network elements comprising the platform at cost-based rates is inconsistent with the Act or undermines the achievement of its purposes would fail. Since Congress required the BOCs to unbundle those elements and adopted a cost-based pricing rule to govern the leasing of network elements, those requirements are entirely consistent with the Act.

2. *Verizon offers no satisfactory response to these arguments.* Verizon's recent letter does not even attempt to come to grips with these arguments. There is no discussion – or even citation – to section 252(a)(1), the provision requiring interconnection agreements to include a list of prices for network elements. Nor is there any discussion – or even citation – to section 252(c)(2), the provision directing state commissions to follow the cost-based pricing rule of section 252(d)(1) when establishing rates for network elements. Nor is there any discussion – or even citation – to the Eighth Circuit's controlling construction of section 251(d)(3), which preserves state authority to establish additional unbundling requirements. Nor is there any discussion – or even citation – to the relevant legislative history (relied on by the Supreme Court) that ties section 271's unbundling requirements to the section 251 process.

More generally, while acknowledging that it erred by arguing that the FCC had *no* authority to set pricing rules, Verizon fails to understand that the 1996 Act did not give *all* authority to the FCC either. Rather, Congress gave the FCC general rulemaking authority and directed the states to arbitrate interconnection agreements. The statute could not be more clear that the state role includes authority to determine whether an incumbent local exchange carrier must lease particular network elements and to establish the price for those elements.

Verizon does not press its argument that BOCs that have obtained authorization to provide long-distance service under section 271 need not provide unbundled access to loops, switching, transport, and signaling pursuant to the checklist. It wisely has receded from its previous claim that those network elements are not "network elements" if the Commission has "delisted" them under section 251(d)(2).[7] There was no merit to that

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[6] *Iowa Utilities Board v. FCC*, 120 F.3d 753, 806-07 (8th Cir. 1997), *not reviewed by AT&T v. Iowa Utilities Board*, 119 S. Ct. 721 (1999).

[7] *See* Verizon comments (Apr. 5, 2002) at 67.

prior argument, since loops, transport, switching and signaling plainly are "network elements." BOCs that have received authorization to provide long-distance service under section 271 therefore must provide unbundled access to those four elements, absent forbearance.[8]

The only issue, therefore, is whether the FCC may order state commissions arbitrating interconnection agreements to disregard Congress's instruction in section 252(c)(2) that network elements be provided at the cost-based rate standard established by section 252(d)(1). All of Verizon's statements to the effect that the FCC has authority to issue pricing rules and the state commissions must follow FCC regulations are irrelevant to that issue. We do not contend and never have contended that the FCC lacks authority to issue pricing rules governing network elements or that the state commissions are not required to follow the FCC's pricing rules. Indeed, we contend that the FCC *has* issued pricing rules implementing section 252(d)(1) (rules that were opposed by the BOCs but upheld by the Supreme Court) and the state commissions *must* follow those rules when establishing rates for network elements (a proposition that also was opposed by the BOCs but upheld by the Supreme Court). Where we part company with Verizon is that we contend that Congress intended the pricing rule it established to govern network elements to be applied when prices are set for network elements.

That conclusion is almost too obvious to dispute, so Verizon never challenges it head on. Verizon instead principally points out that the Commission concluded in 1999 that the pricing rule Congress enacted to govern network elements did not apply to switching provided pursuant to section 271. Of course, that is so, but that is not an answer on the merits. Nor is it a sufficient answer to note that section 252(d)(1) cross-references section 251(c)(3) but not section 271(c)(2)(B). Whatever inferences may be drawn from cross-references in a statute that is not a model of clarity, they cannot override the clear congressional direction to state commissions in section 252(d)(1) to price network elements at cost-based rates, particularly in light of Congress's statement that section 271 sets forth what BOCs must provide in interconnection agreements.[9]

Verizon endorses the Commission's 1999 conclusion that the general pricing rules adopted in 1934 and set forth in sections 201 and 202 should govern network element pricing. And it states that after *Iowa Utilities Board* the "old interstate-intrastate divide ...

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[8] Verizon correctly notes that the statute contemplates that the Commission may forbear from the requirements of the section 271 checklist and that Verizon has asked the Commission to forbear from the checklist items requiring it to unbundle loops, transport, switching, and signaling. Whether BOCs should provide access to those network elements is properly addressed in that separate proceeding. However, as our filings in the forbearance proceeding show, Verizon's forbearance request is grossly premature. *See* Z-Tel's Opposition to Verizon Petition for Forbearance (Sept. 3, 2002).

[9] *See* note 2 and accompanying text, *supra*.

has no operative force with respect to 1996 Act provisions."[10] True enough. But sections 201 and 202 are not "1996 Act provisions" and their reach is explicitly limited to interstate and foreign communications. Verizon also notes that the Supreme Court held (contrary to Verizon's prior position) that the FCC has rulemaking authority with respect to all provisions of the Communications Act. Also true. But the Commission does not have authority to construe the pricing authority in sections 201 and 202, which by their terms apply only to interstate and foreign communications, to cover intrastate communications. The 1996 pricing provision does not have a jurisdictional limit, but the 1934 pricing provision does.

Moreover, Verizon's argument proves too much. If the Supreme Court removed the jurisdictional limits from sections 201 and 202, then the FCC could set end-user rates for local telephone service pursuant to those provisions. Congress did not intend that result and the Supreme Court's decisions do not contemplate that result either. Similarly, the acceptance of Verizon's argument would lead to the conclusion that, contrary to the Supreme Court's decision in *Louisiana Public Service Commission v. FCC*,[11] the FCC may now establish depreciation rates under section 220 that cover intrastate as well as interstate depreciation. But the Supreme Court did not overrule *Louisiana Public Service Commission* in *AT&T Corp. v. Iowa Utilities Board*, it distinguished it on precisely the ground we advance. It held that the FCC has "jurisdiction to make rules governing matters to which the 1996 Act applies," adding that *Louisiana PSC* involved a provision adopted in 1934, and that the FCC "had not explicitly been given rulemaking authority" under the 1934 Act concerning intrastate matters.[12]

In short, if the 1999 pricing rule (section 252(d)(1)) applies, it applies without jurisdictional limitation. But if the 1934 pricing rules (sections 201/202) apply, the FCC's authority is limited to establishing rates for the interstate portions of network elements.[13]

3. *Verizon misunderstands the importance of section 271.* Verizon closes its letter with a confusing argument to the effect that section 271 does not require the BOCs to provide "the so-called UNE-platform."[14] This argument, which repeatedly references the combinations rules, appears to be premised on the "physical" view of unbundling advanced by the BOCs that was explicitly rejected by the Supreme Court in 1999. To "unbundle" does *not* mean to provide in a separated manner, but to provide at a separate price. The Supreme Court so held: "Nor are we persuaded by the incumbents' insistence that the phrase 'on an unbundled basis' in § 251(c)(3) means 'physically separated.' The

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[10] *Verizon letter* at 6.

[11] *Louisiana Public Service Commission v. FCC*, 476 U.S. 355 (1986).

[12] *AT&T Corp.*, *supra*, 525 U.S. at 380 & 381 n.7.

[13] This point is explained in greater detail in Z-Tel's *ex parte* letter filed in this docket on December 20, 2002.

[14] *Verizon letter at 7.*

dictionary definition of 'unbundled' (and the only definition given, we might add) matches the FCC's interpretation of the word: 'to give separate prices for equipment and supporting services.'"[15] The Court added that there was no basis for the BOCs' argument that they could "sabotage network elements" by providing them in physically separate pieces.[16]

Moreover, checklist item two requires BOCs to provide network elements "in accordance with the requirements of sections 251(c)(3) and 252(d)(1)." The first cross-referenced provision is the basis for the rules requiring combinations. The second is the statutory pricing rule, reinforcing the conclusion that the BOCs must provide network elements at cost-based rates. That checklist item is best interpreted as requiring BOCs to unbundle network elements – whether the unbundling requirement was issued pursuant to section 251 or section 271 – at cost-based rates and subject to the combination requirements promulgated pursuant to section 251(c)(3).

Verizon also fails to understand that it is entirely appropriate that section 271 should play a greater role in the Commission's analysis in 2003 than it did in 1996 or 1999.[17] In 1996, of course, no BOC had obtained authorization to provide long-distance service, and it was unclear how many BOCs would seek authorization. When the Commission issued the *UNE Remand Order* in November of 1999, no section 271 petition had yet been granted, although Verizon's petition for New York was pending, and it remained unclear whether some BOCs were seriously interested in obtaining authorization. But 35 section 271 petitions have now been granted. Therefore, the unbundling obligations of BOCs providing long-distance service are now, for the first time, of central importance.

Moreover, the basic scheme of the 1996 Act was that it was designed so that long-distance companies could get into local markets when the BOCs were permitted to get into long-distance. As Senator Breaux stated: "You can get into my business when I can get in your business."[18] As we have explained, the use of the platform permits entry into the local market on the same basis that the BOCs may enter the long-distance market. In the absence of electronic loop provisioning or some other technological advance that makes changing local carriers as easy as changing long-distance carriers, the platform is the only means of providing for parity of entrance into those markets. It therefore is no surprise that Congress placed loops, transport, switching, and signaling on the checklist, and the BOCs sshould not get the benefit of the bargain Congress struck by entering the

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[15] *AT&T Corp.*, *supra*, 525 U.S. at 394.

[16] *Iowa Utilities Board*, *supra*, 119 S. Ct. at 737. This argument was explained in Z-Tel's *ex parte* filing in this docket on January 15, 2003.

[17] However, from the start the Commission recognized that each of those items was on the checklist and concluded that was relevant to determining that each network element ought to be unbundled under section 251. *Local Competition Order*, 11 FCC Rcd 15499 ¶¶ 377 (loops); 410 (switching); 439 (transport); 479 (signaling).

[18] 141 Cong. Rec. S8,153 (daily ed. June 12, 1995) (statement of Senator Breaux).

long-distance market without permitting real competition for mass-market customers in local markets.

Furthermore, it is important to understand that no court reviewing unbundling obligations has had occasion to address section 271. As stated above, the requirements of section 271 were not directly relevant to the FCC's 1996 or 1999 orders because the Commission had not yet granted a section 271 petition. Moreover, and contrary to the implications in Verizon's letter, no court has held under section 251 that loops, transport, switching, or signaling should not be unbundled. The Supreme Court directed the FCC to apply a limiting principle in determining what "impair" means in section 251(d)(2), but it was not asked to decide (and did not decide) whether new entrants would be impaired without those four elements. And contrary to Verizon's contention that section 251(d)(2) is a provision of central importance, the Supreme Court described it as a "curious and isolated" provision.[19] The D.C. Circuit principally directed the Commission to issue rules calling for a more granular analysis[20] – a requirement the BOCs have been running away from as fast as they can – and did not decide whether loops, transport, switching, and signaling should be unbundled under section 251. Indeed, the Commission recognized in its petition for stay of the mandate that "the *USTA* opinion did not even *address* directly the specific network elements" the Commission required all ILECs to unbundle.[21]

A focus on section 271 – now required in light of the many petitions that have been granted – will not answer the question of how the impairment standard should be articulated.[22] But it is relevant to the section 251 inquiry. Congress plainly thought that long-distance companies would be impaired in entering local markets without access to the network elements on the checklist – it explained that the checklist set forth what must, "at a minimum, be provided by a Bell operating company in any interconnection agreement approved under section 251" in order to open its local market to competition.[23] Any impairment standard that reaches a different result with respect to those elements is therefore suspect.

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[19] *AT&T Corp.*, *supra*, 525 U.S. at 381 n.8.

[20] *United States Telecom Association v. FCC*, 290 F.3d 415, 426 (D.C. Cir. 2002); *Competitive Telecommunications Association v. FCC*, 390 F.3d 8, 2002 U.S. App. LEXIS 22407 at *9.

[21] Emergency Consent Motion of the Federal Communications Commission to Extend Partial Stays of Mandates (Dec. 4, 2002), at 6.

[22] As Z-Tel has explained, however, impairment is properly construed as meaning that, without access to a network element, a new entrant's output would be reduced by a significant and non-transitory amount. *See* Z-Tel's reply comments (July 17, 2002) at 21-26.

[23] S. Rep. 104-23, 104th Cong., 1st Sess. 43 (1995).

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Congress established unbundling requirements in 1996 (both with respect to all ILECs in section 251 and with respect to BOCs in section 271) and it established a pricing rule for network elements in 1996 as well (set forth in section 252(d)(1)). In section 252(c)(2), Congress told the state commissions to apply the section 252(d)(1) pricing rule when arbitrating interconnection agreements. The Supreme Court explained that Congress enacted an innovative pricing rule governing network elements in order to provide "every possible incentive" to new entrants to compete with the incumbents, which have "an almost insurmountable competitive advantage."[24] Verizon never responds to these points and never explains why Congress would have enacted a pricing rule for network elements but intended state commissions arbitrating interconnection agreements to ignore it. There is no good answer: Congress plainly intended the pricing rule it adopted to govern network elements to be applied by state commissions arbitrating disputes over rates for network elements.

Sincerely,

/s/

Robert A. Curtis
President, Z-Tel Network Services

Thomas M. Koutsky
Vice President, Law and Public Policy

[24] *Verizon*, *supra*, 122 S. Ct. at 1661, 1662.